Greenspan Ignores Dangerous Trends *Rising Debt to GDP Ratio is a Warning*

Washington, DC: In testimony before the House Financial Services Committee last week, Federal Reserve Chairman Alan Greenspan painted a rosy picture of the U.S. economy. His claim that lower interest rates have strengthened the financial condition of American households deserves closer scrutiny, however.

In fact, Economist Frank Shostak of the Ludwig von Mises Institute throws cold water on the Chairman's assertion:

"According to Greenspan the low interest rate policy of the U.S. central bank has strengthened consumers' and businesses' financial conditions. Our analysis, however, disagrees with this…the data demonstrates that the exact opposite took place."

"Thus the household liabilities-to-assets ratio climbed to a new record high in Q3… Furthermore, the outstanding consumer credit-to-personal income ratio stood at a record…in December. This record high ratio indicates that the pace of consumption by far exceeds the pace of wealth generation. This is likely to force consumers to curtail their borrowing and in turn curtail their expenditure in the months ahead."

"According to Greenspan mortgage refinancing played an important role in last year's buoyant economic growth. (But) how in the world can credit, which is not backed up by real savings, generate economic growth?"

Debt is the fundamental problem that Mr. Greenspan and the central planners at the Fed will not address. The unfavorable ratio of new Treasury debt to GDP has been trending upward for decades. Between 1962 and 1982, the ratio was $1.50/$1 or less. By the mid 1990s, the ratio had grown to about $3/$1. Today the Fed must create nearly $7 of new debt to generate $1 of new GDP.

As financial analyst Jay Taylor explains, this trend illustrates that the only solution federal policy makers know is to print more and more money. Federal debt naturally grows faster than income-- while there are no limits to how fast the printing presses can run, there are natural limits to economic growth.

The end may come when foreign central banks realize the dollars they receive are worthless, or when they find other places to turn for income. When that day comes, interest rates will rise, perhaps dramatically. At that point not even Mr. Greenspan will be able to save the economy from the painful correction necessitated by his easy credit, easy money policies.